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ABSTRACT

A new means of funding school operations known as advanced school funding allows Oklahoma schools financing during the temporary cash shortfalls. The program consists of the Oklahoma Development Authority issuing revenue bonds purchased by E. F. Hutton and Company, Inc., which then sells the tax free bonds to investors throughout the country. A designated trustee bank issues the proceeds of the sale of revenue bonds to purchase nonpayable warrants issued by school districts. The schools are able to use the Oklahoma Development Authority money interest free for 5 and one-half months. The majority of schools place general fund money in certificates of deposit and earn interest from September 1 to February 15. At this time the bank has access to funds from February to September to place in interest bearing accounts for the Oklahoma Development Authority. The bank charges a fee for the trustee services. The most recent issue of notes included 116 districts. (MLF)

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Oklahoma's Advanced School Funding

by

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Introduction

The people of Oklahoma have funded their schools primarily through local support which consists of a 10 mill levy, an emergency levy of 5 mills, and a building fund levy of 5 mills. In addition to these funds the schools acquire other monies through school land, rental and sales, gross production tax, auto licenses, the Rural Electric Association tax, and foundation aid which comes from the state. In addition there are vocational education reimbursements and other special funds from the state and federal programs.

The majority of Oklahoma schools attempt to carry over an excess of 8-10% of the budget each year. However, in the last five years, it has been extremely difficult for some schools to adjust their budgets in order to maintain a financial condition that enables them to have the desired carryover. Poor economic conditions, combined with an unwillingness of the state legislature to change the school finance law has brought about the initiation and growth of a new means of funding school operations known as advanced school funding.

The Oklahoma Development Authority

This funding process is a result of the function of the Oklahoma Development Authority, an Oklahoma public trust. However, the Oklahoma Development Authority was in existence prior to the inception of the Advance Funding Program. Creators of the concept believed that a state-wide public trust would afford certain economies of scale. Any public trust whose powers were sufficiently broad could be the issuing agency for entities within the boundaries of its beneficiary.

The Oklahoma Development Authority was created by and exists under a certain declaration of trust developed in November of 1974. The Oklahoma

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Development Authority was established as a public trust within the state and has as its beneficiary the state of Oklahoma with public purposes as its primary provision. The Oklahoma Development Authority operates under the provision of Title 60, Oklahoma Statutes 1981, Section 146-180.3, enclusive, as an amended act.

The act states that the Oklahoma Development Authority can act for the furtherance and for the convenience of the state and its inhabitants. Furthermore, the Authority is authorized and empowered to provide aid to various municipalities and school districts within state boundaries. The power of the Authority comes through the authorization and empowerment for it to issue revenue bonds or notes to finance the cost of facilities, improvements, buildings and to provide funds which may be necessary or useful, for the provision of services by the state or any municipality or school district. The powers of the Oklahoma Development Authority are very extensive. The declaration which initiated the trust provides that the five trustees of this authority are empowered to purchase, acquire any type of franchises, real or personal property and to enter into various contracts, leases, priviledges, benefits and to pay for the same in cash with bonds or other types of indebtedness.

Therefore, since Oklahoma school districts exist as a corporate body within the state, then the Oklahoma Development Authority is lawfully empowered to issue bonds which can assist in the payment of warrants and claims for the school district.

Financial Scope

During the past four years, several Oklahoma school districts have had an opportunity, through the promotion of E.F Hutton and Company, Inc., to participate in a program which has provided considerable cash benefit to Oklahoma school districts. The Oklahoma Development Authority has provided advanced funding to many school districts. These funds have been used to purchase non-payable warrants issued by the districts.

Each issue of bonds by the Oklahoma Development Authority are rated AAA by Standard and Poors. The first issue of forty-four million in notes in 1982 involved only 3 school districts. The second issue of one hundred and two million included approximately 35 districts in 1983. The most recent issue of 271,325,000 in notes was delivered by the underwriters in February 1985 and included 116 districts. The Oklahoma Development Authority's participation with the Oklahoma school districts in advanced funding has had an explosive growth. It appears to be clear that the participating districts are finding the benefits useful in resolving some of their cash management problems. With program participation these districts have been able to:

1) make purchases when needed rather than when funds are available,
2) improve their cash management,
3) reduce their year-end surpluses
4) improve their bargaining position in regard to their investments.

All of these benefits have been provided to the various school distrcts through the advanced funding program with no cost to the school districts.

How the Program Works

The specifications of the program are fairly complex. The following is a simplified explanation.

The advanced funding concept was the brainchild of E. F. Hutton & Co., Inc. In conjunction with various financial consultants to school districts, Hutton identified a financial need of school districts and outlined a program to help meet monthly obligations. Hutton invited Broken Arrow, Tulsa, and Moore Public Schools to join the experimental proposal. Once the schools had agreed to join the program the total plan was presented to the Oklahoma Development Authority. E.F. Hutton and Company was retained as managing underwriter of the first issue which consisted of approximately 44 million dollars. The Oklahoma Development Authority issued the revenue bonds purchased by E.F.

Hutton and Co. E.F. Hutton in turn sold the tax free bonds to investors throughout the United States. Liberty National Bank & Trust Company was designated as the trustee bank for the advanced funding program. Liberty National Bank used the proceeds of the sale of revenue bonds to purchase non-payable warrants which were issued by the school district. These warrants were purchased on a monthly basis. The period of time for the school districts to issue non-payable warrants was designated from September 1 to February 15. On February 15, the school districts were requried to purchase all of the non-payable warrants from Liberty National Bank. At this time Liberty National Bank had access to funds from February to September to place in interest bearing accounts which made additional money for the Oklahoma Development Authority. Liberty National Bank charges a fee for the trustee services.

The advanced funding concept is a fairly complex financial maneuver. First, there is considerable political element involved as the five appointed trustees have the authority to decide the dollar amount to be issued. Second, E.F. Hutton is placed in a position to profit on this activity primarily based upon the negotiated rate of discount. Third, various investors have an opportunity to save on taxes as a result of purchasing large, tax free, secure and short term revenue bonds. Fourth, Liberty National Bank has had an opportunity to profit as a result of carrying out this acitivity for a negotiated fee. Fifth, the Oklahoma Development Authority has an opportunity to gain access to additional funds as interest is earned on the money in Liberty National Bank from February to September. This money is returned to the Oklahoma Development Authority to be either rebated to participating school districts or used in the furtherance of similar programs. And finally, the public schools have an opportuntiy to profit as a result of being able to use the Oklahoma Development Authority money interest free for five and one-half months. The majority of schools place general fund money in CD's and earn interest from September 1 to February 15. The

amount of interest earned can be very significant depending on the size of the school.

Conclusion

Structurally, tax exempt bonds (such notes are essentially short term, tax free revenue bonds) carry a term of approximately 35 months. Generally speaking, the size of the issue will be determined by trustees of the Oklahoma Development Authority and the provisions of the Internal Revenue Code. Specifically, these provisions allow for financing for the temporary cash shortfalls based on each district's projected monthly income and expenditures and its surpluses at the beginning at each fiscal year. In essence, a shortfall is created when a district's projected income is not sufficient to meet the needs of its estimated expenditure of funds.

The Advanced Funding Program is being sold on the belief that the school district Advanced Program achieves real savings to school districts with only minor changes in bookkeeping and accounting practices. The minor change is basically a substitution of Liberty National Bank as Trustee, as a holder of non-payable warrants for private banking institutions. The program continues to grow in Oklahoma as more schools become involved in the advanced funding process. In general, it seems that it is a opportunity for schools to use non-payable warrants at no interest cost with the opportunity to place some existing school funds on C.D.'s and profit from the program.

References

Parker, Jack and Gene Pingleton, Financing Education in Oklahoma 1985, Oklahoma School Board Association, Oklahoma City, 1985.